First Sentier Equity Income Fund

First Sentier Investors

Formerly the Colonial First State Equity Income Fund-Class A

Quarterly Factsheet

30 September 2022

For Adviser use only

Portfolio Description

This Fund is suitable for investors seeking long term income and reduced volatility from Australian shares.

Investment Strategy

The Fund's returns are generated from a number of sources directly or indirectly, including dividends, franking credits and capital returns from Australian shares, as well as income generated from equity options. The Fund uses equity options to modify the return profile of its Australian share holdings. The use of equity options in conjunction with Australian shares is expected to result in a greater proportion of the total return delivered as income and reduced volatility in returns. In the selection of Australian shares, investment opportunities are identified by detailed fundamental research, including a high number of company visits and utilising a proprietary database to analyse company financials. The Fund predominantly invests in Australian dollar denominated securities and therefore does not hedge currency risk. The Fund uses equity options to modify the return profile of its Australian share holdings, as well as for return enhancement and risk management purposes.

Investment Objective

To provide a total return comprised of regular income, franking credits and some capital growth from Australian shares over the long term, delivered with consistently lower volatility than the S&P/ASX 100 Accumulation Index. The Fund aims to deliver risk adjusted returns that exceed the S&P/ASX 100 Accumulation Index before fees and taxes over a full market cycle.

Key Investment Personnel and Experience (Industry / Firm)

Rudi Minbatiwala	Head of Equity Income	(2000 / 2000)
Jason Moodie	Senior Portfolio Manager	(1995 / 1997)
Marlon Chan	Senior Portfolio Manager	(2007 / 2007)

Product Overview

APIR code	FSF1676AU
Inception date	01 August 2014
Fund Size (A$)	75 million
Benchmark	S&P/ASX 100 Accumulation Index
Number of stock holdings	30
Buy / Sell spread	0.05% / 0.05%
Management fees and costs (p.a.)*	0.96%

* Information on Management fees and costs (including estimated indirect costs) is set out in the Fund's PDS.

Top 10 Active Weight holdings

Stock
CSL
Santos
ResMed
QBE Insurance
James Hardie
Aristocrat Leisure
National Australia Bank
Goodman Group
Computershare
Northern Star Resources

Performance summary (% after fees and expenses)*

Period	3mth	1yr	3yr	5yr	7yr	10yr	SI
Net return	1.4	-8.8	2.9	6.3	6.8	-	5.1
Benchmark return	0.6	-5.9	3.2	7.2	8.2	-	6.5
Excess net return	0.8	-2.9	-0.3	-0.9	-1.4	-	-1.4
Net return (inc. franking)	2.1	-6.4	4.4	8.0	8.5	-	6.8

* Performance is annualised for periods greater than one year.

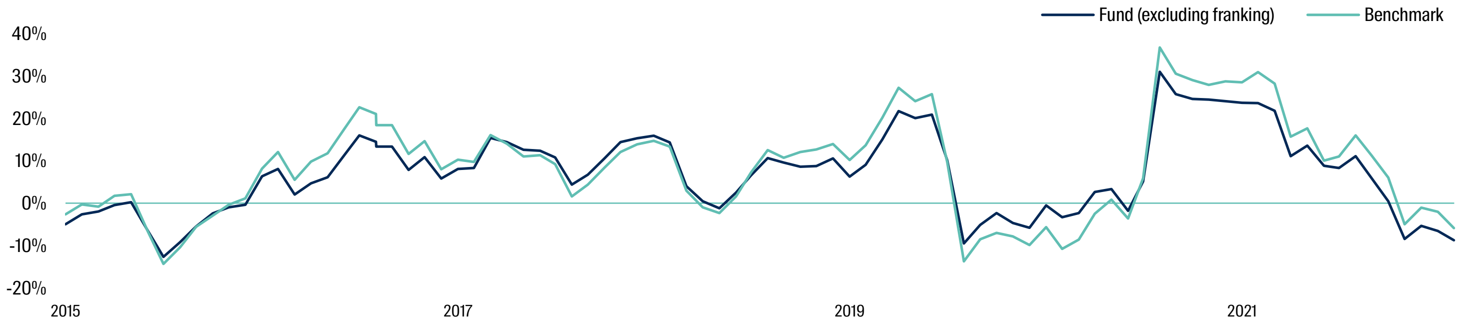
Income summary (% after fees and expenses)

Period	3mth	1yr	3yr	5yr	7yr	10yr	SI
Distribution return (ex. franking)	1.9	7.2	10.7	9.6	9.0	-	8.7
Franking credit return	0.7	2.4	1.5	1.7	1.7	-	1.7

Volatility summary (%)

Period	1yr	3yr	5yr	7yr	10yr	SI
Fund volatility (ex. franking)	13.1	15.6	13.2	12.0	-	12.1
Reference index volatility	15.4	18.5	15.5	14.1	-	14.2

Rolling 1 year return (%)

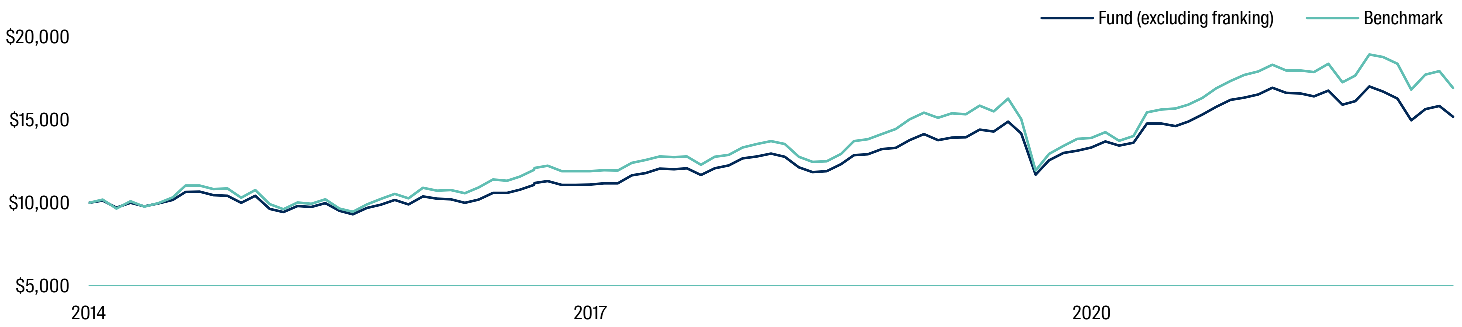


Performance returns are calculated net of management fees and transaction costs. Performance returns for periods greater than one year are annualised. Past performance is not a reliable indicator of future performance.

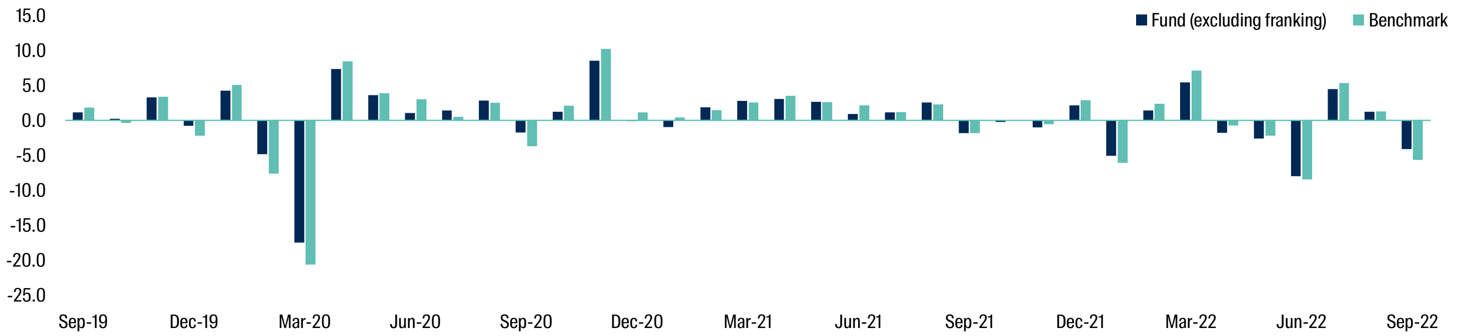
Data source: First Sentier Investors 2022

Data as at: 30 September 2022

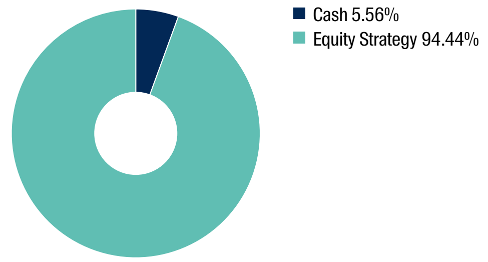
Growth of AUD 10,000 Investment Since Inception



Monthly returns vs benchmark (% excluding franking)



Invested exposure*



*Ignoring options

Market Review

The Australian equity market rose in the first half of the quarter before declining and overall the S&P/ASX 100 Accumulation Index returned +0.6% for the September quarter. The rise at the start of the quarter is attributed to increased traction of the peak inflation and peak monetary policy narrative, and speculation that the US Fed could see a policy pivot in 2023. However, this sentiment soon turned as central bankers pushed back, with Powell's speech at the Jackson Hole emphasising the need to restore price stability and that this could require a restrictive stance for some time. A hotter-than-expected August US inflation print, released in September, undermined conviction in the thesis that inflation has peaked and intensified concerns about an economic hard landing as central banks might have to be more aggressive to bring inflation under control.

Over the quarter, the Reserve Bank of Australia raised rates in three consecutive 50bps raises, to 2.35%, and continued to emphasise their commitment to returning inflation to target over time. They added in their policy statement in September that they would do this while keeping the economy "on an even keel" and the minutes noted members discussed raising interest rates by either 25bps or 50bps, acknowledging that monetary policy operates with a lag and that interest rates had increased quickly and were getting closer to normal settings.

Sectors with long duration real assets were impacted by the rise in bond yields, including the Utilities (-12.5%) and the Real Estate (-6.3%) sector. The Utilities sector is also facing unique challenges presented by the energy transition and the war in the Ukraine which in part is contributing to high volatility in electricity prices. On this backdrop, AGL Energy (-16.0%), APA (-14.9%) and Origin energy (-7.3%) declined.

Energy (+5.1%) was the best performing sector this quarter, boosted by the stellar performance of Whitehaven Coal (+95.6%) which has benefited from rising coal prices as the global energy crises intensifies and pushes up demand for coal. The positive performance of Washington H Soul Pattinson (+13.8%) and Woodside (+4.5%) also added to the sectors performance.

The Information Technology sector's (+4.7%) performance is attributed to the strong rallies experienced by Wisetech (+37.5%) and Altium (+28.9%). Wisetech rallied off the back of a strong FY22 result, with the outlook for next year stronger than expected due to the benefits of continued global roll-outs, cost out and price increases.

Fund Performance

The Fund returned 1.4% for the September quarter, exceeding the benchmark return, which is a pleasing outcome in turbulent market conditions. Performance was improved due to the selective and flexible implementation of sold single stock call options. In the lead up to reporting season, the Fund had a lower option coverage which enabled the Fund to have greater participation when the market experienced a strong rise. Post reporting, option coverage was increased, which provided a substantial cushion as the market sold away.

Stock selection had a roughly neutral contribution to performance over the quarter. Wisetech (WTC) experienced a strong share price appreciation throughout the quarter and contributed strongly to performance. Their FY22 result continued to demonstrate the benefits of focusing upon the top 25 Global Freight Forwarder market, announcing a new global rollout contract with UPS and overall they signed five new global rollouts of their Cargowise product throughout the year. These global rollouts, in addition to any new customers, will continue to drive revenue growth in coming years, with the deep integration of their products and improved customer efficiency providing a significant competitive advantage.

In previous commentaries, we mentioned that we found it surprising that longer dated bond proxy names such as Transurban (TCL) were trading close to all time high valuations despite their negative correlation to interest rates as investors sought out the defensive nature of their inflation linked revenues. These concerns came to pass over the quarter, as the attractiveness of their dividend diminished in the wake of rising yields and they rebased their dividend for FY23 to 53c/share compared to market expectations of 60c/share. The Fund does not hold a position in TCL and hence this contributed positively towards performance.

Our selective positioning within gold stocks added to performance, where the Fund has an overweight position in Northern Star Resources (NST) and nil position in Newcrest Mining (NCM). NST remains a preferred gold exposure within the portfolio because of the more attractive production growth outlook than peers and expectations of a continuation of strong free cash flow generation that saw the company beat expectations at the FY22 result. In addition, NST should be more insulated from cost pressures, as they own a power business in Kalgoorlie and their production growth projects were committed earlier than peers. Further, NST announced an on market share buyback of $300m, reflecting management's confidence in their balance sheet and outlook.

The Fund has no exposure to pure coal companies and as such does not have a position in Whitehaven Coal (WHC) which detracted from performance as coal stocks rallied throughout the quarter. Similarly, lithium exposed stocks experienced large share price appreciations over the quarter as lithium prices soared. We do not hold a position in Mineral Resources (MIN) which detracted from performance, as it experienced a rally due to the upgraded earnings outlook for this segment of their business.

The position in EML payments (EML) detracted from performance as EML confirmed the Central Bank of Ireland has identified shortcomings in the remediation programme which could result in an extended timeline of the programme to meet CBI expectations. This could delay the launch of new programs impacting establishment revenue and GDV growth, with the CBI growth cap potentially being extended. The overweight position in Goodman (GMG) detracted from performance as the real estate sector continues to be impacted by rising bond yields. However, this was somewhat offset as the Fund benefited from a significant underweight position in this sector.

Fund Activity

The Fund initiated a position in medical device company Resmed (RMD) that specialises in the treatment of sleep apnea. Their major competitor Philips was forced to recall products, leaving a major growth opportunity for RMD as they capture Phillips market share. The recall in combination with global chip supply shortages has created a significant backlog of patients as demand outstripped the number of flow machines available. Resmed has had major success in acquiring customers from Phillips recall, and their newly launched card to cloud device has alleviated some of the supply chain constraints and enabled them to meet a greater amount of the patient backlog.

A position was established in Computershare (CPU) over the quarter as their margin income is a significant beneficiary of rising bond yields supporting earnings growth and offsetting inflationary pressures that are impacting costs and the operating business. For context, CPU has estimated its margin income guidance to be ~$520m at the release of their result in August, however with the recent rate rises of ~50bps for FY23 and ~100bps for FY24 the outlook suggests an estimated margin income of $545m for FY23.

The position in Charter Hall (CHC) was exited in preference for Goodman Group (GMG). We believe GMG's higher quality portfolio of industrial assets will be able to drive strong rental growth in comparison to CHC's where exposures to office and retail may slow growth. Rental growth will also be supported by the under-rented portfolio, with market rental rates flowing through as leases roll over. GMG also has an attractive development pipeline, with management expecting that strong rental growth will be able to offset any cost inflation.

Wisetech (WTC) has been a key structural growth position in the portfolio and they remain well placed to deliver strong earnings growth underpinned by their global rollout and recent customer wins. However we partially reduced our holding given the high valuation they were trading at in comparison to peers and the market.

The Fund has long held a position in Amcor (AMC) due to its attractive earnings growth potential derived from the integration of recent acquisitions. The defensive nature of the business has resulted in strong share price appreciation during the recent period of market uncertainty. The Fund exited the position as the earnings outlook had subdued given the realisation of the majority of synergies from the Bemis acquisition and the limited upside for volume growth in a slowing economy.

The position in Domino's (DMP) was exited as ongoing inflationary pressures, particularly rising labour, food input and energy prices, are likely to weigh on margins and earnings. Inflation pressures in combination with lower consumer confidence and decreased profitability may delay franchisees decisions to open new stores which could hamper DMP's store rollout targets.

Market Outlook

Equity markets are likely to experience further volatility as the risk of recession amidst aggressive measures taken by central banks continues to be front of mind for investors. A few months ago we made the observation that P/E multiple compression had been the major cause of the equity market decline and that earnings estimates could be too high. Although some earnings estimates have been pared back following August reporting season, we are conscious of the risk that in light of the outlook for slowing demand and elevated recession risks, earnings estimates still might be too high given demand destruction and margin pressure. Quantitative tightening and rising bond yields are also likely to continue to be headwinds for equity valuations.

Currently many economists are predicting a recession across the US, UK and Europe. However, Australia is regarded to be in a relatively better position to avoid a recession as it benefits from soaring export prices, weaker currency, a very tight labour market and excess savings supporting households. Nonetheless, the risk remains that Australia may not be able to avoid any fallout as high levels of household debt and the impact of a significant property market downturn make Australia more vulnerable. Regardless, we believe that any recession that does eventuate is likely to be highly unique to any type of recession experienced in the past. This recession would be driven by central bank intervention in order to curb inflation in comparison to past recessions that have been credit driven. In this case, it is excess liquidity rather than excess debt, which would contribute to a recession. Further, the strong health of the economy also may indicate that any recession may be less severe, with strong labour dynamics, balance sheets in good shape and tight housing inventories.

In this environment, markets will remain hyper sensitive to economic data releases. It is likely any signs of slowing economy may spark optimism, as it is conflated with the notion that central banks measures have started to work and that this could lead to an earlier slowdown in the pace of tightening. However, any 'relief rally' is likely to be short lived, with price stability likely to remain the key objective for central banks until significant unemployment or declines in growth become a bigger concern. Any data showing more persistent inflation or a stronger economy may contribute to rising recession fears from continued aggressive tightening and could contribute to further equity market falls. The equity income strategy is well placed to navigate the inevitable periods of volatility as this macroeconomic backdrop continues to drive markets. The strategy is able to harness above average levels of volatility to generate higher levels of income and provides a performance cushion during falling markets. Thorough fundamental bottom up stock selection combined with an integrated active option overlay strategy aims to deliver strong through the cycle returns for our investors.

www.firstsentierinvestors.com.au

For further information

Acting Head of Wholesale	
Ross Crocker	+61 2 9010 5424
Key Account Manager - NSW	
Paul Sleiman	+61 2 9010 5393
Business Development Manager – NSW	
Emerson Bloom	+61 2 9010 5547
Key Account Manager - VIC/TAS	
Nick Everitt	+61 3 9225 5055
Business Development Manager - VIC/TAS	
Jack Heinz	+61 3 9225 5056
Key Account Manager - QLD	
Quin Smith	+61 4 5509 5505
Business Development Manager – QLD	
Julie Day	+61 4 6641 3176
Key Account Manager - WA/SA/NT	
Nathan Robinson	+61 4 0327 2440